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Syndicate 1861 Annual Report & Accounts

As at 31 December 2020

Contents

Syndicate 1861

Directors and Professional Advisors

MANAGING AGENT:
Canopius Managing Agents Limited

Directors

N J Betteridge		
P Ceurvorst	Non-Executive Director	
L Davison		
M P Duffy		
P F Hazell	Non-Executive Director	
S Lacy		Appointed 13 July 2020
P Meader	Non-Executive Director	
N S Meyer		
I B Owen	Non-Executive Chairman	
M C Watson		

Company Secretary
P P Hicks

Registered office
Gallery 9
One Lime Street
London
EC3M 7HA

Managing Agent's registration No. 01514453

FCA firm registration No. 204847

SYNDICATE:

Joint Active Underwriters
C Jarvis
S A Willmont

Bankers
Lloyds Bank PLC
Citibank N.A.
Royal Bank of Canada

Investment Manager
BlackRock - 12 Throgmorton Avenue, London, EC2N 2DL

Statutory Auditor
Ernst & Young LLP ("EY")
25 Churchill Place, Canary Wharf, London, E14 5EY

Report of the Directors of the Managing Agent

The directors of Canopius Managing Agents Limited (‘CMA’), the managing agent for Syndicate 1861, present the annual report and audited financial statements for the Syndicate for the year ended 31 December 2020.

These financial statements have been prepared in compliance with United Kingdom Accounting Standards, including Financial Reporting Standard 102, “The Financial Reporting Standard applicable in the United Kingdom and Republic of Ireland” (“FRS102”), Financial Reporting Standard 103, “Insurance Contracts” and the Companies Act 2006. Furthermore, these financial statements comply with the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 ("the 2008 Regulations").

Review of the business

The Syndicate’s principal activity continues to be the transaction of general insurance and reinsurance business at Lloyd’s, transacted through direct channels and via delegated underwriting. The Syndicate capacity for the 2020 year of account was £550m (2019: £500m).

Significant events

With effect from 1 January 2020, in line with the run-off closure plan that they had been operating under since ceasing to underwrite at 1 January 2018, Syndicate 5820’s and Syndicate 1206’s 2017 years of account closed into the 2018 year of account of 1861 by way of a reinsurance to close transaction thus concluding the business of Syndicates 5820 and 1206.

The 2018 year of account in turn has closed externally into the 2021 year of account of Premia Managing Agency Limited’s Syndicate 1884 effective 1 January 2021 following the completion of a reinsurance to close agreement on 18 February 2021.

These transactions represent the completion of Canopius’ strategy to acquire AmTrust at Lloyd’s non-life underwriting participations following both the acquisition of the Syndicate’s capital provider, Flectat 2 Ltd (formerly AmTrust Corporate Member Limited) from the AmTrust group and the novation of the managing agency of the Syndicate from AmTrust Syndicates Limited (‘ASL’) to CMA on 1 October 2019.

The 2020 year of account of Syndicate 1861 was written on a split stamp basis with Syndicate 4444, another Syndicate managed by CMA. Under this arrangement Syndicate 1861 has underwritten 35% of the joint operations.

The Syndicate is not underwriting the 2021 year of account following the pooling of capacity with Syndicate 4444 which will underwrite all risks from the 2021 year of account onwards. Management expect the 2019 year of account of the Syndicate to close into the 2020 year of account in the normal course of business at 31 December 2021 with the 2020 year of account closing into Syndicate 4444’s 2021 year of account a year later thus concluding the business of Syndicate 1861.

Following the UK’s departure from the European Union, and the sanctioning of the scheme by the High Court on 25 November 2020, insurance policies (and related liabilities) underwritten in the European Economic Area (‘EEA’) by the Members and former Members of the Syndicate, as comprised for each of the relevant years of account between 1993 and April 2019 (or October 2020 in the case of German reinsurance), were transferred to Lloyd’s Insurance Company S.A. (‘Lloyd’s Brussels’) together with cash of $63.7m on 30 December 2020 in accordance with Part VII of the Financial Services and Markets Act 2000. On the same date, the Members of the Syndicate entered into a 100% Quota Share Reinsurance Agreement whereby all risks on the same policies were reinsured back from Lloyd’s Brussels to the relevant open years of account of the Syndicate which wrote the transferring policies, and/or inherited liabilities on transferring policies through Reinsurance to Close of earlier years of account, together with an equal amount of cash of $63.7m.

The combined effect of the two transactions had no economic impact for the Syndicate, and accordingly there is no impact on the Syndicate’s income statement, members’ balance or total assets and total liabilities. Both the cash transferred for the Part VII transfer and the premium subsequently received back from Lloyd’s Brussels have been included in the ‘gross written premiums' line of the income statement. This is the appropriate treatment that best reflects the connection between both the Part VII transfer and the associated reinsurance arrangement, and the resulting economic substance of the combined transactions.

Current year underwriting results for the transferred policies have been reported in the same classes of business as in prior years, as the effective date of the transfer was 30 December 2020, and in line with Society of Lloyd's guidance no movements were processed on these policies on 31 December 2020. In future years, results relating to these risks will be reported under the Inwards Reinsurance class of business, reflecting the new contractual arrangement with Lloyd's Brussels.

In addition to the significant financial implications on the Syndicate outlined below, the Covid-19 pandemic has been a huge test of operational resilience. Our Business Continuity Plans proved effective with key systems and processes remaining fully operational whilst the business operated remotely across all regions. We have worked closely with our outsource partners to minimise disruption and ensure services remain in line with existing service level agreements. Our Enterprise Risk Management processes have remained effective throughout the period – there has been no evidence of a deterioration in internal control performance or an increase in risk incidents.

Whilst the business has proven to be resilient, we recognise there is an increased inherent risk in certain areas such as cyber and regulatory risk. In response, additional management actions and controls have been implemented and are closely monitored to address this elevated risk.

The managing agent recognises the great strain that these events have had on our staff and the huge effort that has gone into ensuring the business continues to operate effectively in these unprecedented times. For this we are extremely grateful.

Results and performance - Key performance indicators ('KPIs')

The CMA Board monitors the progress of the Syndicate by reference to the following KPIs:

	2020 £m	2019 £m
Gross premiums written	526.4	661.4
Earned premiums, net of reinsurance	517.5	488.4
Investment return	4.9	11.2
(Loss) / profit for the year	(175.8)	(23.5)
Total comprehensive (loss)/income	(163.0)	(22.0)
Gross claims ratio[1]	95.7%	64.2%
Net claims ratio[2]	91.5%	61.9%
Expense ratios[3]		
- Acquisition ratio	36.1%	37.7%
- Administrative Expense ratio	7.0%	7.2%
Combined operating ratio[4]	134.5%	106.8%
Investment return, on average invested balances[5]	1.5%	3.8%

[1]The gross claims ratio is the ratio of gross claims incurred to gross premiums earned gross of reinsurance and acquisition costs
[2]The net claims ratio is the ratio of net claims incurred to premiums earned net of reinsurance and gross of acquisition costs
[3]The expense ratios are the ratios of the acquisition cost and operating expenses to earned premiums net of reinsurance and gross of brokerage and commissions.
[4]The combined ratio is the ratio of net claims incurred, acquisition costs and net operating expenses to net premiums earned
[5]Investment return is calculated as the combined investment income for the period divided by the average of the opening and closing investments, cash and overseas deposit balances.

The results of the Syndicate for the year are set out on pages 14 and 15. In 2020, Syndicate 1861 recorded a loss of £175.8m (2019: £23.5m loss) with a combined ratio of 134.5% (2019: 106.8%). These results reflect the enormous financial impact of both the Covid-19 pandemic and a record breaking hurricane season in terms of frequency, producing the largest number of named storms ever. The effect of these events was to worsen the net claims ratio by 29.6% to 91.5%, compared with the previous year (2019: 61.9%).

Whilst more positive underwriting conditions emerged in many sectors during 2020 as rates hardened, underwriting discipline was maintained with the Syndicate scaling back in poorly performing non-core lines and growing where real value can be achieved. There was a marked change in business mix for the 2020 year of account following the novation of the Syndicate from AmTrust to CMA in October 2019, as the Syndicate wrote on a split-stamp basis with CMA's other non-life Syndicate, Syndicate 4444. As a result of this combination, the optimisation of the overall portfolio and the effects of the pandemic, gross written premium reduced to £526m (2019:£661m).

The key driver of the Syndicate results was the net claims performance. Claims in respect of the Covid-19 pandemic total £128m net of reinsurance recoveries, adding 27% to the net loss ratio. The discontinued Contingency class, written on the 2018 and 2019 years of account, was the most severely impacted line as a result of the large number of event cancellations following the restrictions imposed in an effort to contain the virus. Given the ongoing nature of the pandemic, there remains uncertainty around the ultimate cost of claims on this book.

Other classes were also impacted, to a lesser extent, as a result of business interruption (UK Property and Treaty Property classes), the recessionary impacts of the pandemic following the sharp decline in economic activity (Casualty, Political Risk and Treaty classes) as well as from an increase in medical expenses and travel related claims (Accident and Health).

Catastrophe experience in the year was heavier than expectation and whilst no single loss would be considered market changing on its own, there was a marked increase in the frequency of events contributing 10.7% to the net claims ratio. The Syndicate's biggest exposure to these was through hurricane Laura (net incurred claims of £21.5m). Additionally, the Syndicate was exposed to Hurricanes Zeta and Sally as well as to a number of smaller US weather events including the Midwest Derecho storm and several instances of tornadoes and hail storms.

Syndicate 1861's investment portfolio achieved a return of £4.9m in 2020 (2019: £11.2m). The previous year's results benefitted from the reversal of prior mark-to-market losses predominantly on the US fixed interest portfolio following material reductions in interest rates. Whilst 2020 saw further rate reductions as fiscal stimulus packages were implemented across major economies, the change was not as pronounced as in 2019. The portfolio has been positioned defensively to protect against volatility during a turbulent year for financial markets, moving into 2021 the Board seeks to maximise the return on the investable portfolio within the Syndicate's risk appetite with a focus on capital preservation and the need to maintain liquidity.

The 2018 year of account of Syndicate 1861 closed with a reported loss of £55.7m representing a loss of 10.3% on managed capacity.

Business environment

2020 was marked by a series of exceptional events, testing the financial and operational resilience of businesses across the world. The most significant of these being the Covid-19 global pandemic, but we have also seen continued global trade tensions, a divisive US presidential election campaign, civil unrest and a record-breaking Atlantic hurricane season.

The pandemic has led to significant stress on health systems and prompted widespread shutdowns across the globe. Despite the resulting economic impact, financial market performance was surprisingly positive. There was volatility throughout the year as markets reacted to good and bad Covid-19 news, but confidence has been steadfast in the fundamentals of the economy.

Uncertainty remains high as we navigate through a deep global recession, and the pace and path of the recovery will depend on many factors, including the requirement for continued restrictions, the degree of economic scarring, and government fiscal stimulus. Interest rates look likely to remain low and continue to suppress investment income and for the UK there is the additional uncertainty resulting from its departure from the European Union. There remains optimism that mass vaccinations will enable life to return towards normality at some point during 2021.

In general insurance markets, hard market conditions persist and have accelerated post Covid-19 with double-digit rate increases being seen across the majority of Property and Casualty classes. This has led to an influx of capital to the sector, particularly for London and Bermuda focussed businesses.

Significant losses relating to Covid-19 have been felt across multiple classes including contingency, trade credit and liability lines. Other lines are also experiencing significant reductions in premium income. In the UK, the Financial Conduct Authority (FCA) Business Interruption test case has led to material pay-outs for non-damage property business interruption exposures. This is not restricted to the UK as other territories undertake similar review processes to bring clarity to the interpretation of policy wordings.

On top of Covid-19 related losses, the market has experienced significant aggregate losses from natural catastrophes. As well as destructive fires and record heat, the active Atlantic hurricane season generated multiple hurricanes and tropical storms. The industry experienced the largest number of named storms on record (thirty) with Hurricane Laura being the most severe with industry losses estimated at around $10bn.

As well as the ongoing focus on conduct and operational resilience, regulators continue to closely monitor capital and liquidity levels to ensure financial market soundness and stability. Regulators are also playing an active role in climate change which is just one factor in a wide range of Economic, Social and Governance (ESG) issues which are becoming increasing important for businesses to incorporate into business strategies.

Principal risks and uncertainties

The process of risk acceptance and risk management is addressed through a framework of policies, procedures and internal controls. All policies are subject to Board approval and ongoing review by management, risk management and internal audit. The Audit Committee is responsible for satisfying itself that a proper internal control framework exists to manage financial risks and that controls operate effectively.

CMA's governance structure ensures a clear definition of responsibility for the management and oversight of the many risks faced by the business. CMA has established an Enterprise Risk Management (ERM) framework that is designed to identify, assess, measure, mitigate, monitor and report all material financial and non-financial risk.

The managing agent has identified the following principal risks and uncertainties facing the Syndicate as detailed in Note 5 to the financial statements (management of risk):

- Insurance risk
- Financial risk
    - i. Market risk
    - ii. Credit risk
    - iii. Currency risk
    - iv. Liquidity risk
- Group risk
- Operational risk
- Regulatory risk

Report of the Directors of the Managing Agent

Strategy and future developments

Following the decision to concentrate underwriting into Syndicate 4444 for the 2021 year of account, the strategy for the Syndicate has shifted to the effective management of the run off of the business prior to closure and conclusion of the Syndicate expected 31 December 2022.

Going concern

After making enquiries, the directors have a reasonable expectation that continued capital support will be in place such that the Syndicate is able to support the in-force business in the open underwriting years of account. Accordingly, they continue to adopt the going concern basis in preparing the annual financial statements.

Directors

The directors of the managing agents who served from 1 January 2020 to the date of this report are shown on page 2. None of the directors had an allocated premium limit on the Syndicate, on either an unlimited or limited liability basis, for any of the 2018 to 2020 years of account.

Statement of disclosure of information to auditors

In the case of each of the persons who are directors of the managing agent at the time the report is approved:

- So far as the director is aware, there is no relevant audit information, being information needed by the Syndicate's auditor in connection with the auditor's report, of which the auditor is unaware; and
- Having made enquiries of fellow directors of the agency and the Syndicate's auditor, each director has taken all the steps that he or she ought to have taken as a director to become aware of any relevant audit information and to establish that the Syndicate's auditor is aware of that information.

Statement of Managing Agent's Responsibilities

The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 require the directors of the managing agent to prepare syndicate annual accounts each year which give a true and fair view, in accordance with applicable law and United Kingdom Generally Accepted Accounting Practice, of the state of affairs of the syndicate and of the profit or loss of the syndicate for that period. In preparing those financial statements, the managing agent is required to:

- Select suitable accounting policies and then apply them consistently;
- Make judgements and estimates that are reasonable and prudent;
- State whether applicable UK accounting standards have been followed, subject to any material departures disclosed and explained in the syndicate accounts; and
- Prepare the syndicate accounts on the basis that the syndicate will continue to write future business unless it is inappropriate to do so.

The managing agent confirms that it has complied with the above requirements in preparing the syndicate accounts. The directors of the managing agent are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the syndicate and enable it to ensure that the syndicate accounts comply with the 2008 Regulations. The managing agent is also responsible for safeguarding the assets of the syndicate and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The managing agent is responsible for the maintenance and integrity of the corporate and financial information included on the business' website. Legislation in the United Kingdom governing the preparation and dissemination of annual accounts may differ from legislation in other jurisdictions.

Report of the Directors of the Managing Agent

Independent Auditors

In accordance with section 14(2) of Schedule 1 of the Lloyd's Regulations 2008, the auditor, Ernst & Young LLP, will be deemed to be reappointed and therefore continue in office.

By order of the Board of the managing agent.

N S Meyer
Chief Financial Officer
London, 4 March 2021

Independent Auditor's Report to the Members of Syndicate 1861

for the year ended 31 December 2020

Opinion

We have audited the syndicate annual accounts of syndicate 1861 ('the syndicate') for the year ended 31 December 2020 which comprise the Income Statement, the Statement of Changes in Members' Balances, the Statement of Financial Position, the Statement of Cash Flows and the related notes 1 to 29, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards including FRS 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland' and FRS 103 'Insurance Contracts' (United Kingdom Generally Accepted Accounting Practice).

In our opinion, the syndicate annual accounts:

- give a true and fair view of the syndicate's affairs as at 31 December 2020 and of its loss for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the syndicate annual accounts section of our report. We are independent of the syndicate in accordance with the ethical requirements that are relevant to our audit of the syndicate annual accounts in the UK, including the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

In auditing the syndicate annual accounts, we have concluded that the managing agent's use of the going concern basis of accounting in the preparation of the syndicate annual accounts is appropriate.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the syndicate's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from when the syndicate annual accounts are authorised for issue.

Our responsibilities and the responsibilities of the managing agent with respect to going concern are described in the relevant sections of this report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the syndicate's ability to continue as a going concern.

Other information

The other information comprises the information included in the Annual Report and Accounts, other than the syndicate annual accounts and our auditor’s report thereon. The directors of the managing agent are responsible for the other information.

Our opinion on the syndicate annual accounts does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the syndicate annual accounts or our knowledge obtained in the course of the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the syndicate annual accounts themselves. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

Opinions on other matters prescribed by The Insurance Accounts Directive (Lloyd’s Syndicate and Aggregate Accounts) Regulations 2008

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the managing agent’s report for the financial year in which the syndicate annual accounts are prepared is consistent with the syndicate annual accounts; and
- the managing agent’s report has been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the syndicate and its environment obtained in the course of the audit, we have not identified material misstatements in the managing agent’s report.

We have nothing to report in respect of the following matters where The Insurance Accounts Directive (Lloyd’s Syndicate and Aggregate Accounts) Regulations 2008 requires us to report to you, if in our opinion:

- the managing agent in respect of the syndicate has not kept adequate accounting records; or
- the syndicate annual accounts are not in agreement with the accounting records; or
- certain disclosures of the managing agents’ emoluments specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Independent Auditor's Report to the Members of Syndicate 1861

for the year ended 31 December 2020

Responsibilities of the directors of the managing agent

As explained more fully in the Statement of Managing Agent's Responsibilities set out on page 7, the managing agent is responsible for the preparation of the syndicate annual accounts and for being satisfied that they give a true and fair view, and for such internal control as the managing agent determines is necessary to enable the preparation of the syndicate annual accounts that are free from material misstatement, whether due to fraud or error.

In preparing the syndicate annual accounts, the managing agent is responsible for assessing the syndicate's ability to continue in operation, disclosing as applicable, matters related to its ability to continue in operation and using the going concern basis of accounting unless the managing agent either intends to cease to operate the syndicate, or has no realistic alternative but to do so.

Auditor's responsibilities for the audit of the syndicate annual accounts

Our objectives are to obtain reasonable assurance about whether the syndicate annual accounts as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these syndicate annual accounts.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect irregularities, including fraud. The risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

The extent to which our procedures are capable of detecting irregularities, including fraud, is detailed below. However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the managing agent and management.

Our approach was as follows:

- We obtained a general understanding of the legal and regulatory frameworks that are applicable to the syndicate and determined that the most significant are direct laws and regulations, related to elements of Lloyd's Byelaws and Regulations, and the financial reporting framework (UK GAAP), and requirements referred to by Lloyd's in the instructions. Our considerations of other laws and regulations that may have a material effect on the syndicate annual accounts included permissions and supervisory requirements of Lloyd's of London, the Prudential Regulation Authority ('PRA') and the Financial Conduct Authority ('FCA').

- We obtained a general understanding of how the syndicate is complying with those frameworks by making enquiries of management, internal audit, and those responsible for legal and compliance matters of the syndicate. In assessing the effectiveness of the control environment, we also reviewed significant correspondence between the syndicate, Lloyd's of London and other UK regulatory bodies; reviewed minutes of the Board and Risk Committee of the managing agent; and gained an understanding of the managing agent's approach to governance.

- For direct laws and regulations, we considered the extent of compliance with those laws and regulations as part of our procedures on the related syndicate annual accounts' items.

- For both direct and other laws and regulations, our procedures involved: making enquiry of the directors of the managing agent and senior management for their awareness of any non-compliance of laws or regulations, inquiring about the policies that have been established to prevent non-compliance with laws and regulations by officers and employees, inquiring about the managing agent's methods of enforcing and monitoring compliance with such policies, inspecting significant correspondence with Lloyd's, the FCA and the PRA.

- The syndicate operates in the insurance industry which is a highly regulated environment. As such the Senior Statutory Auditor considered the experience and expertise of the engagement team to ensure that the team had the appropriate competence and capabilities, which included the use of specialists where appropriate.

- We assessed the susceptibility of the syndicate's annual accounts to material misstatement, including how fraud might occur by considering the controls that the managing agent has established to address risks identified by the managing agent, or that otherwise seek to prevent, deter or detect fraud. We also considered areas of significant judgement, including complex transactions, performance targets, external pressures and their potential to influence management to manage earnings or influence the perceptions of stakeholders. The fraud risk was considered to be higher within the valuation of gross incurred but not reported reserves and estimated premium income.

Our audit procedures included:

- Reviewing accounting estimates for evidence of management bias. Supported by our Actuaries we assessed if there were any indicators of management bias in the valuation of gross incurred but not reported reserves and the recognition of estimated premium income.

- Evaluating the business rationale for significant and/or unusual transactions.

- Testing the appropriateness of journal entries recorded in the general ledger, particularly in respect of judgemental areas including gross incurred but not reported reserves and estimated premium income.

In addition, we considered the impact of Covid-19 on the syndicate, including an assessment of the consistency of operations and controls in place as they transitioned to operating remotely for a significant proportion of 2020, making enquiries with management via the use of video conferencing. We performed analytical review procedures to assess for unusual movements throughout the year. Our audit procedures also incorporated unpredictability into the nature, timing and extent of our testing.

A further description of our responsibilities for the audit of financial statements is located on the Financial Reporting Council's website at https://www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Independent Auditor's Report to the Members of Syndicate 1861

for the year ended 31 December 2020

Use of our report

This report is made solely to the syndicate's members, as a body, in accordance with The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008. Our audit work has been undertaken so that we might state to the syndicate's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the syndicate and the syndicate's members as a body, for our audit work, for this report, or for the opinions we have formed.

Michael Purrington (Senior statutory auditor)

for and on behalf of Ernst & Young LLP, Statutory Auditor

London

4 March 2021

Income Statement: Technical Account – General Business

for the year ended 31 December 2020

	Notes	2020 £000	2020 £000	2019 £000	2019 £000
Earned premiums, net of reinsurance					
Gross premiums written	7	526,427		661,367	
Outward reinsurance premiums		(119,095)		(135,961)	
Net premiums written		407,332		525,406	
Change in the provision for unearned premiums:					
Gross amount	24	132,236		(49,748)	
Reinsurers' share	24	(22,083)		12,703	
Change in the net provision for unearned premiums		110,153		(37,045)	
Earned premiums, net of reinsurance			517,485		488,361
Allocated investment return transferred from the non-technical account	14		4,868		11,162
Claims incurred, net of reinsurance					
Claims paid					
Gross amount		(350,920)		(190,429)	
Reinsurers' share		55,448		53,546	
Net claims paid		(295,472)		(136,883)	
Change in the provision for claims					
Gross amount	24	(279,444)		(202,344)	
Reinsurers' share	24	101,263		36,774	
Change in the net provisions for claims		(178,181)		(165,570)	
Claims incurred, net of reinsurance			(473,653)		(302,453)
Net operating expenses	10, 11		(222,580)		(219,243)
Balance on the technical account for general business			(173,880)		(22,173)

The Syndicate has ceased trading forward and therefore there are no component parts of the business to be separately classified and disclosed as discontinued.

Income Statement: Non-technical Account

for the year ended 31 December 2020

	Notes	2020 £000	2019 £000
Balance on the general business technical account		(173,880)	(22,173)
Investment income	14	5,302	3,048
Realised gains on investments	14	667	6,072
Net unrealised gains / (losses) investments	14	(1,101)	2,397
Investment expenses and charges	14	-	(355)
Allocated investment return transferred to the general business technical account		(4,868)	(11,162)
Loss on exchange	10	(1,894)	(1,329)
Loss for the year		(175,774)	(23,502)
Other comprehensive income - Currency translation differences		12,803	1,546
Total comprehensive loss for the year		**(162,971)**	**(21,956)**

The Syndicate has ceased trading forward and therefore there are no component parts of the business to be separately classified and disclosed as discontinued.

Statement of Change in Members' Balances

for the year ended 31 December 2020

	2020 £000	2019 £000
Members' balances at 1 January	(21,964)	(30,748)
Total comprehensive loss for financial year	(162,971)	(21,956)
Amount received from members' personal reserve fund	764	30,748
Movement in non-standard personal expenses	10	(8)
Members' balances at 31 December	**(184,161)**	**(21,964)**

Statement of Financial Position – Assets

at 31 December 2020

	Notes	2020 £000	2020 £000	2019 £000	2019 £000
Investments					
Other financial investments	15		301,721		212,467
Reinsurers' share of technical provisions					
Provision for unearned premiums	24	40,237		63,204	
Claims outstanding	24	205,737		98,844	
			245,974		162,048
Debtors					
Debtors arising out of direct insurance operations	16	179,712		314,742	
Debtors arising out of reinsurance operations	17	107,621		25,948	
Other debtors	18	5,182		712	
			292,515		341,402
Other assets					
Cash at bank and in hand			48,876		75,694
Overseas deposits	19		40,509		35,731
Prepayments and accrued income					
Deferred acquisition costs	23	103,621		126,688	
Other prepayments and accrued income		1,991		2,997	
			105,612		129,685
Total assets			1,035,207		957,027

Statement of Financial Position – Liabilities

at 31 December 2020

	Notes	2020 £000	2020 £000	2019 £000	2019 £000
Capital and reserves					
Members' balances	2		(184,161)		(21,964)
Technical provisions					
Provision for unearned premiums	24	314,376		387,735	
Claims outstanding	24	770,971		456,646	
			1,085,347		844,381
Creditors					
Creditors arising out of direct insurance operations	20	34,888		43,362	
Creditors arising out of reinsurance operations	21	82,848		75,394	
Other creditors	22	16,241		15,854	
			133,977		134,610
Accruals and deferred income			44		-
Total liabilities			1,035,207		957,027

The financial statements on pages 14 to 44 were approved by the Board of CMA on 4 March 2021 and were signed on its behalf by:

N S Meyer
Chief Financial Officer
4 March 2021

Statement of Cash Flows

for the year ended 31 December 2020

	2020		*2019*	
	£000	***£000***	*£000*	*£000*
Cash flows from operating activities				
Loss for the year	(175,774)		(23,502)	
Increase / (decrease) in gross technical provisions	240,966		(28,460)	
(Increase) / decrease in reinsurers' share of gross technical provisions	(83,926)		56,346	
Decrease / (increase) in debtors	48,887		(79,504)	
(Decrease) / increase in creditors	(633)		47,892	
Movement in other assets/liabilities	19,339		10,822	
Investment return	(4,868)		(11,162)	
Foreign exchange	13,401		5,502	
Net cash (outflows) / inflows from operating activities		57,392		(22,066)
Cash flows from investing activities				
Purchase of equity and debt instruments	(210,037)		(409,757)	
Sale of equity and debt instruments	119,682		454,790	
Investment income received	5,969		8,765	
Net cash inflows / (outflows) from investing activities		(84,386)		53,798
Cash flows from financing activities				
Amount received from members' personal reserve funds	774		30,748	
Net cash inflows from financing activities		774		30,748
Foreign exchange on cash and cash equivalents	(598)		(3,956)	
Other	-		(8)	
Net increase / (decrease) in cash and cash equivalents		(26,818)		58,516
Cash at bank and in hand				
Cash and cash equivalents at beginning of year		75,694		17,178
Cash at bank and in hand				
Cash and cash equivalents at end of year		48,876		75,694

1. Statement of compliance & basis of preparation

These financial statements have been prepared in compliance with United Kingdom Accounting Standards, including Financial Reporting Standard 102, "The Financial Reporting Standard applicable in the United Kingdom and Republic of Ireland" ("FRS102"), Financial Reporting Standard 103, "Insurance Contracts" and in accordance with the provisions of Schedule 3 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations relating to insurance companies. Furthermore, these financial statements comply with the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 ("the 2008 Regulations"). The directors of the managing agent have prepared the financial statements on the basis that the syndicate is able to support the business in the open years of account for the foreseeable future.

The financial statements are prepared under the historical cost convention except for certain financial instruments which are measured at fair value.

The financial statements are presented in sterling, the presentation currency, and rounded to the nearest £'000. The functional currency of the syndicate is US dollars.

As permitted by FRS 103 the Syndicate continues to apply the existing accounting policies that were applied prior to this standard for its insurance contracts.

2. Members' balances and Funds at Lloyd's ("FAL")

The members' balances on the balance sheet shows a deficit of £184.2m (2019: deficit £22.0m). The ability of the Syndicate to meet its obligations as they fall due is underpinned by the members' Funds at Lloyd's and the support provided by the Lloyd's chain of security for any members who are unable to meet their underwriting liabilities. FAL is further explained in Note 29.

3. Summary of significant accounting policies

a. Insurance contracts

Insurance contracts (including inwards reinsurance contracts) are defined as those that transfer significant insurance risk. Insurance risk is considered significant if, and only if, an insured event could cause an insurer to pay significant additional benefits above the premiums received and interest earned thereon, excluding scenarios that lack commercial substance. Such contracts remain insurance contracts until all rights and obligations are extinguished or expire.

Contracts that do not transfer significant insurance risk are accounted for as financial transactions. The Syndicate adopts an annual basis of accounting for insurance contracts whereby the incurred cost of claims, commissions and related expenses are charged against the earned proportion of premiums, net of reinsurance.

Gross premiums written, stated gross of acquisition costs and exclusive of premium taxes, relate to business incepted during the year and adjustments to premiums booked in prior years and includes estimates, based on underwriting estimates or past experience, of premiums due but not yet receivable or notified to the syndicate by intermediaries. Additional or return premiums are treated as a re-measurement of the initial premium.

Gross premium written in 2020 include negative premiums for the consideration paid in relation to the business transferred to Lloyd's Brussels on 30 December 2020, this is offset by an equal inwards reinsurance premium received from Lloyd's Brussels on the same date.

Unearned premiums represent the proportion of premiums written that relate to unexpired terms of policies in force at the balance sheet date, calculated by reference to the expected incidence of risk over the period of cover.

Written outwards reinsurance premiums comprise the total premiums payable for contracts entered into during the period and are recognised on the date on which the policy incepts.

3. Summary of significant accounting policies (continued)

a. Insurance contracts (continued)

Premiums include any adjustments arising in the accounting period in respect of reinsurance contracts incepting in prior accounting periods.

Under some policies, reinsurance premiums payable are adjusted retrospectively in the light of claims experience. Where written premiums are subject to a re-measurement retrospectively they are recognised as soon as there is an obligation to the reinsurer.

Outwards reinsurance premiums are accounted for and earned in the same accounting period as the premiums for the related direct or inwards business being reinsured within the parameters of the reinsurance contract terms. The provision for reinsurers' share of unearned premiums represents that part of reinsurance premiums written which is estimated to be earned in the following financial years.

There are a number of different types of business written by the syndicate, including property, liability and marine business, broadly categorised as either "short tail" or "long tail" business. The syndicate also writes reinsurance business. The characteristics of this business mirror those of the underlying business ceded to the syndicate.

The accounting policies for insurance claims and claims settlement expenses are considered in Note 4 (Critical accounting judgements and estimation uncertainty).

Short Tail Business

For "short tail" business there is typically no significant delay between the occurrence of the claim and the claim being reported. The costs of claims notified at the balance sheet date are estimated on a case-by-case basis to reflect the individual circumstances of each claim. The ultimate expected cost of claims, including provisions for claims incurred but not reported ("IBNR"), is projected from this data by reference to statistics, which show how estimates of claims incurred in previous periods have developed over time.

Longer tail business

For longer tail business there is typically a delay between the occurrence of a claim and the claim being reported. Consequently a larger element of the claims provision relates to IBNR claims. Claims estimates for business in this category are derived from a combination of loss ratio based estimates and estimates based upon actual claims experience, using a predetermined formula whereby greater weight is given to actual claims experience as time passes. The initial estimates of the claims provisions are based on the experience of previous years and benchmarks adjusted for factors such as premium rate changes and claims inflation. For liability claims, the assessment of claims is particularly sensitive to the level of court awards and to the development of legal precedent on matters of contract and tort. The liability classes of business are also subject to the emergence of new types of latent claims.

b. Unexpired risk reserves

At each balance sheet date tests are performed to ensure the adequacy of the unearned premium reserve, net of associated deferred acquisition costs, to cover future claims liabilities. In performing these tests, estimates of future premiums and claims cash flows, claims handling expenses and investment income from the assets backing such liabilities are considered and compared to the balances in the unearned premium reserve and deferred acquisition costs. Provision is made for any deficiencies by establishing an unexpired risk reserve.

Unexpired risk surpluses and deficits are offset where business classes are managed together and a provision is made if an aggregate deficit arises. Unexpired risk reserves, where relevant, are included within "claims outstanding" in the balance sheet. At 31 December 2020 the Syndicate did not have an unexpired risks provision (31 December 2019: £Nil)

c. Deferred acquisition costs

Acquisition costs comprise costs arising from the inception of insurance contracts. They include both direct costs, such as intermediary commissions and indirect costs, such as the administrative expenses associated with the issuing of policies. Deferred acquisition costs represent the proportion of commission and other acquisition costs relating to policies in force at the period-end, that cover subsequent reporting periods. These are amortised over the period in which the related premiums are earned.

3. Summary of significant accounting policies (continued)

d. Reinsurance to close ("RITC")

Each syndicate's underwriting year of account is normally closed after the end of the third year by means of reinsurance into the following underwriting year of account, which reinsures all liabilities for the closed year in return for a premium determined by the syndicate's managing agent.

Third party RITCs, either inwards or outwards, are not reported as income but recognised as a transfer of assets and liabilities.

e. Outwards reinsurance contracts

Outwards reinsurance contracts are contracts entered into by the syndicate with reinsurers whereby the syndicate may recover a proportion of losses on contracts written by the syndicate. Contracts that do not transfer significant insurance risk are accounted for as financial transactions.

The benefits to which the syndicate is entitled under its outwards reinsurance contracts are recognised as reinsurance assets. These assets consist of short term balances due from reinsurers as well as longer term receivables that are dependent on the expected claims and benefits arising under the related insurance contracts. These balances are based on calculated amounts of outstanding claims and projections for IBNR, having regard to the reinsurance programme in place for the class of business and the claims experience for the period, net of estimated irrecoverable amounts after assessing the current security rating of the reinsurer involved. Reinsurance liabilities are primarily premiums payable for reinsurance contracts.

The syndicate assesses its reinsurance assets for impairment. If there is evidence of impairment, then the carrying amount is reduced to its recoverable amount and the impairment loss is recognised in the profit and loss account.

f. Receivables and payables related to insurance contracts

Receivables and payables include amounts due to and from agents, brokers and insurance contract holders. If there is evidence that the insurance receivable is impaired, the Syndicate reduces the carrying amount of the insurance receivable accordingly and recognises that impairment loss in the profit and loss account.

g. Financial assets

The Syndicate states financial assets at fair value.

The Syndicate classifies its financial assets into the following categories: financial assets at fair value through profit and loss, and loans and receivables. The Syndicate does not invest in derivative financial instruments and there are no assets classified as available for sale.

The classification depends on the purpose for which the investments were acquired. Management determines the classification of its investments at initial recognition.

Financial assets and liabilities are offset and the net amount reported in the balance sheet only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

(i) Financial assets at fair value through profit and loss

The Syndicate classifies its investments at fair value through profit and loss.

Purchases and sales of investments are accounted for at their fair values (normally their cost of acquisition or proceeds of disposal) on the trade date, which is the date the Syndicate commits to purchase or sell the assets.

The fair value of quoted investments is based on quoted bid prices. Realised and unrealised gains and losses arising from the changes in fair values are included in investment return in the profit and loss account in the period in which they arise. Unquoted investments are initially carried at cost as the best estimate of fair value, which is adjusted using appropriate valuation techniques and having regard to subsequent events or changes in circumstances.

3. Summary of significant accounting policies (continued)

g. Financial assets (continued)

Realised gains and losses on investments carried at market value are calculated as the difference between sale proceeds and purchase price. Unrealised gains and losses on investments represent the difference between the valuation at the balance sheet date and their valuation at the previous balance sheet date, or purchase price, if acquired during the year, together with the reversal of unrealised gains and losses recognised in earlier accounting periods in respect of investment disposals in the current period.

Investment return is initially recorded in the non-technical account. A transfer is made from the non-technical account to the general business technical account. Investment return has been wholly allocated to the technical account as all investments relate to the technical account.

(ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, are not intended to be sold in the short term and do not fall into the other categories of financial assets as described above. Loans and receivables are measured at fair value. Appropriate allowances for estimated irrecoverable amounts are recognised in the profit and loss account when there is objective evidence that the syndicate will not be able to collect all amounts due according to their original terms. These are reversed if the payment is received. Receivables arising from insurance contracts are classified in this category and are reviewed for impairment as part of the impairment review of loans and receivables.

(iii) Deposits with ceding undertakings

Syndicate 1861 advances funds to ceding undertakings for the settlement of claims. These are measured at cost less allowance for impairment.

(iv) Derivative financial instruments

Syndicate 1861 enters into exchange traded derivatives and foreign currency forward contracts from time to time to manage its exposures to interest rate risk and foreign exchange rate volatility. These contracts are initially recorded at cost and revalued to their fair value at each period end by reference to the rates of exchange ruling at the balance sheet date. Any gains or losses on the contracts are included in the non-technical account.

(v) Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities.

Lloyd's overseas deposits are not included within the balance of cash at bank and in hand on the Balance Sheet. These are recognised separately in their own category within other assets.

h. Foreign currencies

In accordance with FRS102, the functional currency is the currency of the primary economic environment in which the syndicate operates. The functional currency for Syndicate 1861 is the US Dollar. The statutory report and accounts are presented in Sterling. Foreign exchange resulting from translating balances in functional currency into Sterling is recorded through Other Comprehensive Income. FRS 102 requires all foreign currency transactions to be translated into the functional currency at the transactional rate of exchange. Transactions in Sterling, Canadian dollars, Euros and Australian dollars are translated to US Dollars at the average rates of exchange for the period. Underwriting transactions denominated in other foreign currencies are included at the rate of exchange ruling at the date the transaction is processed.

At the period end, the monetary foreign currency items are translated to US Dollars at the closing rate with any difference being recorded in the non-technical account. For the purposes of applying the requirements of Section 30 Foreign Currency Translation of FRS 102, all assets and liabilities arising from insurance contracts are treated as monetary items.

3. Summary of significant accounting policies (continued)

i. Taxation

Under Schedule 19 of the Finance Act 1993 managing agents are not required to deduct basic rate income tax from trading income. In addition, all UK basic rate income tax deducted from syndicate investment income is recoverable by managing agents and consequently the distribution made to members is gross of tax. Capital appreciation falls within trading income and is also distributed gross of tax.

No provision has been made for any United States federal income tax payable on underwriting results or investment earnings. Any payments on account made by the Syndicate during the year have been included in the balance sheet under the heading “other debtors”. No provision has been made for any other overseas tax payable by members on underwriting results.

4. Critical accounting judgements and estimation uncertainty

Insurance claims and claims settlement expenses

Insurance claims and claims settlement expenses comprise claims and related expenses paid in the year and changes in the provisions for outstanding claims, including provisions for IBNR and related expenses, together with any other adjustments to claims from prior years.

Provision is made at the period-end for the estimated cost of claims incurred but not settled at the balance sheet date, including the cost of claims incurred but not yet reported to the Syndicate. The estimated cost of claims includes expenses to be incurred in settling claims and a deduction for the expected value of salvage and other recoveries. There is inherent uncertainty in establishing claims provisions and it is likely that the final outcome will prove to be different from the original estimate of the liability. Adjustments to the amounts of claims provisions established in prior years are included in the financial statements in the period in which the adjustments are made. The claims provisions are reviewed regularly.

Estimating claims IBNR is inherently more uncertain than the cost of claims notified, for which more information about the claim event is generally available.

Classes of business where the IBNR proportion of the total claims provisions is high will typically display greater variations between initial estimates and final outcomes because of the greater degree of difficulty of estimating these reserves. Classes of business where claims are typically reported relatively quickly after the claim event tend to display lower levels of volatility in the claims provisions.

Where possible the Syndicate adopts multiple techniques to estimate the required level of claims provisions. This assists in giving greater understanding of the trends inherent in the data being projected. The projections given by the various methodologies also assist in setting the range of possible outcomes. The most appropriate estimation technique is selected taking into account the characteristics of the business class and the extent of the development of each underwriting year of account.

Allowance is made for changes or uncertainties which may create distortions in the underlying statistics or which might cause the cost of unsettled claims to increase or reduce when compared with the cost of previously settled claims including:

- changes in the business environment or processes which might accelerate or slow down the development and/or recording of paid or incurred claims compared with the statistics from prior periods;
- changes in the legal environment;
- the effects of inflation;
- changes in the mix of business;
- the impact of large losses; and
- movements in industry benchmarks.

4. Critical accounting judgements and estimation uncertainty (continued)

Insurance claims and claims settlement expenses (continued)

A component of these estimation techniques is usually the estimation of the cost of notified but not paid claims. In estimating the cost of these the Syndicate has regard to the claim circumstance as reported, any information available from loss adjusters and information on the cost of settling claims with similar characteristics in previous periods.

Large claims and catastrophe events impacting each relevant business class are generally assessed separately, being measured on a case-by-case basis or projected separately in order to allow for the possible distortive effect of the development and incidence of these large claims.

Claims provisions are calculated gross of any reinsurance recoveries. A separate estimate is made of the amounts that will be recoverable from reinsurers. An assessment is also made of the recoverability of reinsurance recoveries having regard to available data on the financial strength of each of the reinsurance companies.

Claims reserved as non-life annuities are discounted for investment earnings that may be expected to arise in the future on funds retained to meet the future liabilities. All other claims provisions are undiscounted.

Premium estimates

Gross written premiums include an estimate of the total premiums expected to be received under each insurance and reinsurance contract. Revenue recognised on policies written through contracts with third parties, such as binding authorities and line slips, is calculated based on the estimated underlying inception profile of each contract and, therefore, this premium recognition is judgmental. Further adjustments to estimates from previous years are also included in the reported premiums for the relevant underwriting years.

Reinstatement premiums are estimated in accordance with the contract terms and recorded based upon paid losses and claims reserves.

Premium estimation uses expert judgement, the quality of the estimate being influenced by the nature and maturity of the portfolio, availability of timely data, relevant underwriting input to the estimating process and management review. Gross written premium estimates are reviewed regularly using underwriter estimates and actuarial projections.

Financial investments

The Syndicate uses prices provided by third party suppliers, investment managers and counterparty banks in determining the fair value of financial assets. Depending on the methods and assumptions used, for example, in the fair valuation of Level 2 and Level 3 financial assets, the fair valuation can be subject to estimation uncertainty. These methods and assumptions are described in Note 5 below.

5. Management of risk

The Syndicate has identified the principal risks and uncertainties arising from its activities and has established policies and procedures to manage these items in accordance with its risk appetite. The sections below explain how the Syndicate defines and manages each category of risk.

a. Insurance risk

Insurance risk is defined as the risk of fluctuations in the timing, frequency and severity of insured events and claims settlements, relative to expectations. Syndicate 1861's exposure to insurance risk arises from underwriting/pricing, insurance concentrations, reserving and reinsurance. The Board of CMA seeks to mitigate insurance risk by analysing historical pricing and claims experience, setting a tolerance to concentration risk, monitoring performance, and conducting in-house actuarial reviews of claims provisions, independent of the underwriting teams.

The Syndicate has formal controls in place to ensure that business is underwritten in a controlled environment by reference to both the annual business plan and in line with underwriting policy. Preventative controls include underwriting authority limits which are agreed and signed off by the Active Underwriter, divisional and Group underwriting guidelines and benchmark ratings for

5. Management of risk (continued)

a. Insurance risk (continued)

all underwriting divisions. Detection controls include exception reports where authority limits are exceeded, expert review procedures, peer reviews and internal audit reviews.

Syndicate 1861 is exposed to potentially significant losses arising from natural catastrophe events such as windstorm, earthquake, flood or pandemic in addition to man-made perils. CMA quantifies catastrophe risk exposures using proprietary modelling software in conjunction with the principal underwriting systems to assess and model catastrophe exposures. The modelling tools are used in conjunction with CMA's knowledge of the business, historical loss information and geographic accumulations to monitor aggregation and to simulate catastrophe losses. The range of scenarios considered includes natural catastrophe, property, marine, liability and terrorism events.

CMA's capital setting methodology enables modelling to be performed in a sophisticated, but practical, manner particularly in determining the correlations between catastrophe exposed classes of business. Stochastic models use event tables which capture directly the different geographic distributions of risk in the various lines of business.

Effective risk management in non-core areas and from non-modelled perils is ensured using a suite of exposure accumulation and aggregation monitoring techniques and proprietary deterministic models.

As a guide to the level of concentration of exposure the Syndicate writes, the following table shows the Syndicate's 1:100 probabilistic modelled exposure to its three largest natural catastrophe perils during 2020:

Peril	Gross Loss £m	Final Net Loss £m
North Atlantic Hurricane	338	95
US Earthquake	195	30
North America Tornado	56	15

The managing agent manages insurance risks on behalf of the Syndicate, including the following:

- inappropriate underwriting activities and cycle management;
- inadequate catastrophe exposure management; and
- inadequate or insufficient reinsurance protection.

The underwriters, supported by the actuarial pricing team, use their expertise and experience to determine the likely claims cost and, therefore, the premium that should be sufficient (across a portfolio of risks) to cover claims costs, expenses and to produce an acceptable profit in line with the agreed business plan.

Due to the nature of insurance risk, however, the premium charged may not be sufficient to cover the cost of claims. The shortfall may result from insufficient premium being calculated and charged or from an unexpected or unprecedented high level of claims.

A number of controls are employed to limit insurance exposures. Each year a business plan is prepared and agreed by the Board which sets the premium income targets and exposures to be written in total and for each class of business. Progress against this plan is monitored by the Board during the year.

Insurance liabilities are assumed through individual risk acceptances, reinsurance treaties or binding authorities. Binding authorities delegate underwriting authority to other underwriters, or agents acting as coverholders, who use their judgement to write risks on Syndicate 1861's behalf under clear authority levels. In such situations, the coverholders' activities are closely monitored and reviewed, and periodic on-site audits are carried out to ensure that the terms of the delegated authorities are being adhered to.

5. Management of risk (continued)

a. Insurance risk (continued)

The Syndicate is also exposed to the risk of:

- inappropriate claims reserves;
- inappropriate payment of claims.

All claims arising are reserved upon notification. The entire portfolio of business is subject to a quarterly reserving process whereby levels of paid and outstanding claims are reviewed. Potential future claims are assessed with a provision for IBNR claims being made. The quarterly review process is overseen by the Reserving Committee. Whilst a detailed and disciplined reserving exercise is carried out, known claims can develop beyond the level of reserves held.

Furthermore, there is increased uncertainty around the provision for IBNR claims. Consequently, there is a possibility that claims may arise which in aggregate exceed the reserve provision established. In the event that claims do not develop in line with expectations, the Reserving Committee will seek to release any redundant reserves.

The Syndicate purchases specific reinsurances to protect against single risk losses. The Syndicate also purchases general excess of loss reinsurance to protect from severe losses. The structure of the programme and type of protection bought will vary from year to year depending on risk appetite and the availability and price of cover.

(i) Development of claims

The claims provisions established can be more or less than adequate to meet eventual claims. The level of uncertainty varies from class to class but can arise from inadequate case reserves for known large losses and catastrophes or from inadequate provision for IBNR. The impact on profit of a 1% improvement/deterioration in the total net claims reserves would be a £5.7m gain/loss (2019: £3.6m gain/loss).

(ii) Claims development tables

The development of insurance liabilities provides a measure of the syndicate's ability to estimate the ultimate value of claims. Historic development includes a mix of prior year releases and deteriorations, and in 2020 gross and net deteriorations occurred. Claims development is expected over the first 3 years of a year of account as the business written, and as yet unwritten, writes and earns. The tables below are presented at the exchange rates prevailing at 31 December 2020.

At 31 December 2020 **Gross of reinsurance**	***2017[1]*** ***£000***	***2018*** ***£000***	***2019*** ***£000***	***2020*** ***£000***	***Total*** ***£000***
At end of underwriting year	99,926	136,910	136,746	156,171	529,753
One year later	189,977	351,900	442,343	-	984,220
Two years later	211,875	455,133	-	-	667,008
Three years later	465,836	-	-	-	465,836
Gross ultimate claims on premium earned to date	465,836	455,133	442,343	156,171	1,519,483
Cumulative payments	(351,282)	(242,160)	(133,466)	(21,604)	(748,512)
Gross claim reserve	114,554	212,973	308,877	134,567	770,971

At 31 December 2020 **Net of reinsurance**	***2017[1]*** ***£000***	***2018*** ***£000***	***2019*** ***£000***	***2020*** ***£000***	***Total*** ***£000***
At end of underwriting year	63,824	109,188	107,408	120,081	400,501
One year later	136,758	269,716	345,162	-	751,636
Two years later	158,070	337,879	-	-	495,949
Three years later	360,464	-	-	-	360,464
Net ultimate claims on premium earned to date	360,464	337,879	345,162	120,081	1,163,586
Cumulative payments	(271,986)	(188,898)	(116,411)	(21,057)	(598,352)
Net claim reserve	88,478	148,981	228,751	99,024	565,234

[1]The 2018 Year of account of Syndicate 1861 accepted the RITC of the 2017 Years of account of Syndicate 5820 and 1206 effective 1 January 2020. The assumed reserves have been disclosed within the 2017 year of account above under "three years later" resulting in an apparent significant development in claims in respect of the 2017 YOA.

5. Management of risk (continued)

b. Financial risk

The Syndicate is exposed to a wide range of financial risks, the key financial risk being that the proceeds from its assets are not sufficient to fund the obligations arising from its insurance contracts. An analysis of the Syndicate's exposure to the significant components of financial risk is given below split between:

(i) Market risk (including interest rate risk and equity price risk);
(ii) Credit risk (including Fair Value Hierarchy);
(iii) Currency risk; and
(iv) Liquidity risk.

(i) Market risk

Market risk arises from fluctuations in values of, or income from, assets or in interest or exchange rates and is derived primarily from the Syndicate's investment of trust fund monies and from currency exposures. The Board has agreed an investment strategy commensurate with the Syndicate's risk appetite.

Interest rate risk

CMA manages sensitivity to market conditions by reference to interest rate risk. Since the majority of the Syndicate's investments comprise cash, overseas deposits and fixed income securities, the fair value of the portfolio is inversely correlated to movements in interest rates. If interest rates fall, the fair value of the Syndicate's fixed income securities tends to rise and vice versa. The fair value of fixed income investments in the Syndicate's balance sheet at 31 December 2020 was £137.6m (2019: £158.3m) with an average duration 2.4 years (2019: 3.0 years). If interest rates were to rise/(fall) by 50 basis points at the balance sheet date, the fair value and therefore the profit for the financial year and members' balances would decrease/(increase) by approximately £1.8m (2019: £1.7m).

The Syndicate manages interest rate risk by investing in financial investments, cash and overseas deposits with an average duration of less than four years. The Investment Committee monitors the duration of these assets on a regular basis.

Outstanding claims provisions are not sensitive to the level of interest rates as they are undiscounted and contractually non-interest bearing.

(ii) Credit risk

Credit risk is the risk that the Syndicate becomes exposed to loss if a counterparty fails to perform its contractual obligations. Credit risk could, therefore, impact upon the Syndicate's ability to meet its claims as they fall due. The Syndicate has in place policies and procedures designed to manage its credit risk exposures.

The primary sources of credit risk for the Syndicate are:

- amounts due from reinsurers,
- amounts due from insurance intermediaries, and
- counterparty risk with respect to investments including cash and cash equivalents.

The credit risk in respect of reinsurance debtors is primarily managed by review and approval of reinsurance security by CMA's Reinsurance Security Committee, prior to the purchase of reinsurance contracts. Guidelines are set and monitored, that limit the purchase of reinsurance based on Standard & Poor's or appropriate alternative ratings for each reinsurer. The credit risk in respect of reinsurers is primarily managed by CMA's reinsurance support team. Provisions are made against the amounts due from certain reinsurers, depending on the current rating assigned to the reinsurer. Some reinsurers provide collateral, either through deposits held in designated trust accounts or through letters of credit, to protect the Syndicate in the event of non-payment of debt. As this collateral effectively guarantees the debt, these reinsurers are zero-rated for bad debt provisions. The recovery of debt from reinsurers is administered by the credit management team.

The credit risk in respect of insurance intermediaries is managed by the credit management function with the aid of the underwriting support team and a dedicated binder management team.

Notes to the Financial Statements

for the year ended 31 December 2020

5. Management of risk (continued)

(ii) Credit risk (continued)

To transact business with the Syndicate the insurance intermediary must first comply with internal guidelines that include approval (where relevant) by both the PRA and Lloyd's, to have a satisfactory credit rating and to have in place a terms of business agreement or a binding authority agreement with the Syndicate. The position is then monitored through ongoing review of the amount of debt outstanding to terms, and by regular cover-holder audits.

The Finance Group regularly reviews inwards premiums debtors and reinsurance debtors by reference to the age of the debt. The objective of the Finance Group is to ensure robust balance sheet management, financial accounting and regulatory reporting oversight and to maintain a strong governance and control framework.

Debts from insurance intermediaries fall due according to the terms of trade; debts from reinsurers crystallise in line with the reinsurance contract terms.

An analysis of amounts past due from insurance intermediaries and reinsurers by age is presented below.

At 31 December 2020	***Neither past due nor impaired***	***Up to 3 months***	***3 – 6 months***	***6 – 12 months***	***More than 12 months***	***Total***
	£000	***£000***	***£000***	***£000***	***£000***	***£000***
Debtors arising out of direct insurance operations	179,712	-	-	-	-	179,712
Debtors arising out of reinsurance operations[1]:						
Due from intermediaries under reinsurance business	81,293	-	-	-	-	81,293
Reinsurance recoverables on paid claims	-	10,882	9,377	3,848	2,221	26,328
Total	261,005	10,882	9,377	3,848	2,221	287,333

[1]Debtors arising out of reinsurance operations include future premiums due on inwards reinsurance that would previously have been included as arising from direct insurance operations. In 2019 £61.9m of accepted reinsurance pipeline debtors were included in debtors arising out of direct insurance operations in this regard. The comparatives have not been restated as we do not believe the reclassification would influence the economic decisions of users and is therefore not considered material.

At 31 December 2019	***Neither past due nor impaired***	***Up to 3 months***	***3 – 6 months***	***6 – 12 months***	***More than 12 months***	***Total***
	£000	***£000***	***£000***	***£000***	***£000***	***£000***
Debtors arising out of direct insurance operations	313,928	814	-	-	-	314,742
Debtors arising out of reinsurance operations:						
Due from intermediaries under reinsurance business	963	-	-	-	-	963
Reinsurance recoverables on paid claims	-	15,839	5,904	2,475	767	24,985
Total	314,891	16,653	5,904	2,475	767	340,690

Credit risk within the investment funds is managed through the credit research carried out by the investment managers. The investment guidelines are designed to mitigate credit risk by setting minimum credit worthiness of investments and ensuring diversification of the holdings.

5. Management of risk (continued)

(ii) Credit risk (continued)

An analysis of the Syndicate's major exposure to counterparty credit risk and credit risk with the investment funds and cash, based on Standard & Poor's or equivalent rating, is presented below. These assets are neither overdue nor impaired.

At 31 December 2020	***AAA***	***AA***	***A***	***BBB/ BB***	***Other/Not rated***	***Total***
	£000	***£000***	***£000***	***£000***	***£000***	***£000***
Reinsurers' share of claims outstanding	-	21,329	172,613	1,854	9,941	205,737
Debt and other fixed income securities	27,969	37,293	44,257	28,109	-	137,628
Shares and other variable yield securities and units in unit trusts	154,271	-	-	-	8,403	162,674
Derivative assets	-	-	-	-	1,419	1,419
Overseas deposits	24,529	3,305	8,088	2,618	1,969	40,509
Cash	-	-	48,876	-	-	48,876
Total	206,769	61,927	273,834	32,581	21,732	596,843

At 31 December 2019	***AAA***	***AA***	***A***	***BBB/ BB***	***Other/Not rated***	***Total***
	£000	***£000***	***£000***	***£000***	***£000***	***£000***
Reinsurers' share of claims outstanding	-	7,488	86,100	-	5,256	98,844
Debt and other fixed income securities	20,600	51,246	34,783	51,631	-	158,260
Shares and other variable yield securities and units in unit trusts	52,174	-	2,033	-	-	54,207
Overseas deposits	22,349	3,880	6,609	2,829	64	35,731
Cash	-	-	75,694	-	-	75,694
Total	95,123	62,614	205,219	54,460	5,320	422,736

The carrying values represent the maximum exposure to credit risk at the balance sheet date in respect of the above assets. The analysis above does not include insurance debtors from direct insurance operations as the majority of these assets are in respect of premiums for which the information is not readily available. Those reinsurance reserves with unrated counterparties are fully collateralised.

Fair Value Hierarchy

The Syndicate has classified its financial instruments in accordance with the requirements of paragraph 16 to the March 2016 amendment to FRS102 and has adopted an approach consistent with IFRS13, Fair Value Measurement. The fair value hierarchy classifies financial instruments into Level 1 to 3 based on the significance of the inputs used in measuring their fair value.

The levels within the fair value hierarchy are defined as follows:

- Level 1 - Based on unadjusted quoted price in an active market for identical assets or liabilities that the entity can access at the measurement.
- Level 2 - Based on inputs other than quoted prices included within Level 1 that are observable (i.e. developed using market data) for the asset or liability, either directly or indirectly.
- Level 3 - Where inputs are unobservable (i.e. for which market data is unavailable) for the asset or liability.

5. Management of risk (continued)

Fair Value Hierarchy (continued)

At 31 December 2020	***Level 1***	***Level 2***	***Level 3***	***Total***
	£000	***£000***	***£000***	***£000***
Shares and other variable yield securities	19,913	134,358	8,403	162,674
Debt and other fixed income securities	2,048	135,580	-	137,628
Derivative assets	-	1,419	-	1,419
Other financial investments	21,961	271,357	8,403	301,721
Overseas Deposits	10,798	29,711	-	40,509
Derivative liabilities	-	(393)	-	(393)
Total	32,759	300,675	8,403	341,837

At 31 December 2019	***Level 1***	***Level 2***	***Level 3***	***Total***
	£000	***£000***	***£000***	***£000***
Shares and other variable yield securities	-	52,174	2,033	54,207
Debt and other fixed income securities	19,539	138,721	-	158,260
Other financial investments	19,539	190,895	2,033	212,467
Overseas Deposits	9,102	26,629	-	35,731
Total	28,641	217,524	2,033	248,198

The level within the hierarchy that a financial instrument is placed is based on the lowest level of any input that is significant to its fair value measurement. Quoted prices for corporate bonds are based on a limited number of transactions for those securities and as such are considered to meet the definition of level 2 assets.

Values for assets which have no observable market are considered level 3 assets. This balance represents the loan to the central fund where a fair value adjustment has been applied. The fair value of the loan at year end is £8.4m (2019: £2.0m). No further level 3 disclosure is provided on the grounds of materiality.

(iii) Currency risk

Policyholders' assets are held in the five principal Lloyd's settlement currencies (Sterling, Euros, US, Australian and Canadian dollars) which represent the vast majority of the Syndicate's liabilities by currency. A significant proportion of the Syndicate's business is transacted in US dollars. The Syndicate's functional currency is US dollars and, therefore, foreign exchange risk also arises when non-US dollar profits are converted into US dollars.

CMA has a group policy to mitigate foreign exchange risk and this policy is managed by the Finance team and overseen by the Finance Group which is headed by the CFO.

The Syndicate is exposed to foreign exchange risk primarily with respect to the Sterling, Euro Australian and Canadian dollar. The Syndicate mitigates this risk by endeavouring to match assets and liabilities in foreign currency. The Managing Agent's Finance Group reviews currency matching quarterly.

In certain circumstances, the Syndicate is exposed to a subsidiary foreign exchange risk where regulators demand that the Syndicate holds US, Australian and Canadian dollar currency assets to match liabilities measured on a regulatory basis, rather than best estimate.

For the avoidance of doubt, the Syndicate is not positioned to take speculative currency positions to make gains; the purpose of its foreign exchange risk policy is to protect against the downside.

5. Management of risk (continued)

(iii) Currency risk (continued)

The profile of the Syndicate's assets and liabilities, categorised by currency, was as follows:

At 31 December 2020	***Sterling & Other***	***US dollar***	***Euro***	***CAD***	***AUD***	***Total***
	£000	***£000***	***£000***	***£000***	***£000***	***£000***
Financial investments	37,394	193,397	29,613	41,317	-	301,721
Overseas deposits	12,825	4,303	-	7,938	15,443	40,509
Reinsurers' share of technical provisions	15,163	213,993	13,265	2,196	1,357	245,974
Insurance and reinsurance receivables	44,159	206,114	27,507	5,049	4,504	287,333
Cash and cash equivalents	6,864	1,971	36,063	-	3,978	48,876
Other assets	52,242	42,859	13,137	1,876	680	110,794
Total assets	168,647	662,637	119,585	58,376	25,962	1,035,207
Technical provisions	(187,259)	(750,150)	(95,827)	(27,793)	(24,318)	(1,085,347)
Insurance and reinsurance payables	(11,235)	(93,880)	(7,996)	(1,872)	(2,753)	(117,736)
Other creditors	(12,902)	(3,319)	(64)	-	-	(16,285)
Total liabilities	(211,396)	(847,349)	(103,887)	(29,665)	(27,071)	(1,219,368)

At 31 December 2019	***Sterling & Other***	***US dollar***	***Euro***	***CAD***	***AUD***	***Total***
	£000	***£000***	***£000***	***£000***	***£000***	***£000***
Financial investments	13,747	148,296	26,423	24,001	-	212,467
Overseas deposits	13,674	3,246	-	4,697	14,114	35,731
Reinsurers' share of technical provisions	5,532	144,760	8,517	2,216	1,023	162,048
Insurance and reinsurance receivables	49,348	247,076	26,656	9,336	8,274	340,690
Cash and cash equivalents	27,308	34,895	10,217	-	3,274	75,694
Other assets	52,035	60,191	11,381	4,149	2,641	130,397
Total assets	161,644	638,464	83,194	44,399	29,326	957,027
Technical provisions	(157,125)	(560,763)	(76,454)	(26,287)	(23,752)	(844,381)
Insurance and reinsurance payables	(7,954)	(97,528)	(7,278)	(2,584)	(3,412)	(118,756)
Other creditors	(15,651)	(203)	-	-	-	(15,854)
Total liabilities	(180,730)	(658,494)	(83,732)	(28,871)	(27,164)	(978,991)

5. Management of risk (continued)

(iv) Liquidity risk

Liquidity risk arises where insufficient financial resources are maintained to meet liabilities as they fall due.

All valid claims must be paid as they fall due and, therefore, it is essential that the Syndicate maintains an appropriate level of liquidity at all times. As a consequence, cash is managed closely by the Treasury team. The Syndicate is exposed to daily calls on its available cash resources, principally from claims arising from its insurance activities.

The Syndicate's policy is to manage its liquidity position so that it can reasonably meet a significant individual or market loss event. This means that the Syndicate maintains sufficient liquid assets, or assets that can be quickly converted into liquid assets, without any significant capital loss, to meet estimated cash flow requirements. The availability of liquidity in the event of a major disaster is regularly tested using internal cash flow forecasts and realistic disaster scenarios.

The majority of the Syndicate's investments are in highly liquid assets which could be converted into cash promptly and at minimal expense. Cash and overseas deposits are generally bank deposits and money market funds.

In addition, the duration of assets is maintained at a level to manage liability durations and in recognition of the Syndicate's catastrophe exposures. Greater levels of cash and/or liquid assets may be held when determined by market conditions and is considered appropriate by the Chief Investment Officer.

The tables below show the maturity profile of the Syndicate's financial liabilities.

At 31 December 2020	*No stated maturity*	*0-1 year*	*1-3 years*	*3-5 years*	*>5 years*	*Total*
	£000	*£000*	*£000*	*£000*	*£000*	*£000*
Derivative liabilities	-	393	-	-	-	393
Creditors	-	133,584	-	-	-	133,584
Claims outstanding	-	285,882	283,518	115,104	86,467	770,971
Total	-	419,859	283,518	115,104	86,467	904,948

At 31 December 2019	*No stated maturity*	*0-1 year*	*1-3 years*	*3-5 years*	*>5 years*	*Total*
	£000	*£000*	*£000*	*£000*	*£000*	*£000*
Creditors	-	134,610	-	-	-	134,610
Claims outstanding	-	154,231	179,474	73,755	49,186	456,646
Total	-	288,841	179,474	73,755	49,186	591,256

5. Management of risk (continued)

c. Group risk

Group risk arises from the potential impact of risk events, of any nature, arising in or from membership of a corporate group. CMA is part of the Canopius Group Limited ("CGL"), a global underwriter of insurance and reinsurance business transacted both through direct channels and via delegated underwriting. CGL has established a risk management framework to protect the Group's stakeholders, including Syndicate members from events that hinder the sustainable achievement of financial performance objectives, including failing to exploit opportunities. Management recognises the critical importance of having efficient and effective risk management systems in place.

A clear organisational structure is in place with delegated authorities and clear responsibilities. A Group policy framework is in place which sets out the risk management, internal control and business conduct standards for the Group's operations. Group risk management policies set out the identification of risk and its interpretation, limit its structure to ensure the appropriate quality and diversification of assets, align underwriting and reinsurance strategy to the corporate goals, and specify reporting requirements. Each policy has a member of senior management charged with overseeing compliance throughout the Group and the CGL Board meet regularly to approve any commercial, regulatory and organisational requirements of such policies.

d. Operational risk

Operational risk is the risk of inadequate or failed internal processes, people and systems, or external events that have an adverse impact on the business. The Syndicate manages these risks through a framework of robust systems and controls. CMA's objective for operational risk management is to identify, assess, manage, monitor and report risks and to prevent or reduce any failures or inadequacies in systems and controls. To this end, CMA has established key policies and controls that include:

- regular meetings of the Board of directors at which key aspects of the managing agent's and Syndicate's businesses are reviewed, including review of reports from various sub-committees of the Board
- underwriting procedures guidelines
- claims management policies and guidelines
- risk registers which are reviewed and signed off by the risk and control owners on a regular basis
- a suite of risk policies for major risk categories relating to the activities of the Syndicate
- an internal audit function whose audit plan is aligned with CMA's risk framework
- human resources policies and guidelines designed to ensure that the operations are adequately resourced by sufficiently skilled and trained people, who are appropriately remunerated
- financial policies and controls that cover:
    - maintaining segregated funds for the Syndicate's assets
    - investment of funds
    - expense management
    - establishing adequate provisions for unpaid claims
    - credit risk, including debt collection and managing counter-party exposures
    - cash flow and other financial projections
    - regular review and reconciliation of the entity's financial records.

In addition, the managing agent has an established and integrated capital and planning cycle. This provides an assessment of the significant financial and non-financial risks, as identified by the managing agent's risk management framework. The capital requirement is assessed in accordance with applicable requirements through the use of deterministic and stochastic modelling and further challenged using a comprehensive validation process which includes the use of stress and scenario tests. This process assesses the capital required to meet a 1 in 200 level extreme outcome from the aggregation of all recognised sources of risk.

5. Management of risk (continued)

e. Regulatory risk

Regulatory risk is the risk that the Syndicate fails to meet the regulatory requirements of the Prudential Regulatory Authority ("PRA"), the Financial Conduct Authority ("FCA"), Lloyd's and those of overseas regulators in jurisdictions where Lloyd's syndicates are licensed to trade.

Regulatory risk is a key area of focus for the Risk and Compliance teams to ensure legislative and regulatory changes are understood and observed.

6. Capital setting, capital management policies and objectives

The Syndicate's objectives in managing its capital are to:

- satisfy the requirements of its policyholders and regulators; and
- allocate capital efficiently to support strategic objectives.

The Society of Lloyd's applies capital requirements at member level and in aggregate to ensure that Lloyd's complies with all regulatory requirements such as Solvency II, whilst meeting its own financial strength, licence and ratings objectives.

Although Lloyd's capital setting processes use a capital requirement set at syndicate level as a starting point, the requirement to meet Solvency II and Lloyd's capital requirements apply at overall and member level only respectively, not at syndicate level. Accordingly the capital requirement in respect of Syndicate 1861 is not disclosed in these financial statements.

The PRA and Lloyd's oversee the capital setting regime that requires syndicates to calculate their own capital requirements through a Solvency Capital Requirement ("SCR"). The SCR must be sufficient to cover a 1 in 200 year loss, reflecting uncertainty in the ultimate run-off of underwriting liabilities (SCR 'to ultimate'). The syndicate must also calculate its SCR at the same confidence level but reflecting uncertainty over a one year time horizon (one year SCR) for Lloyd's to use in meeting Solvency II requirements. The SCRs of each syndicate are subject to review by Lloyd's and approval by the Lloyd's Capital and Planning Group.

A syndicate may be comprised of one or more underwriting members of Lloyd's. Each member is liable for its share of underwriting liabilities on the syndicate(s) on which it participates but not other members' shares. Accordingly, the capital requirement that Lloyd's sets for each member, operates on a similar basis. Each member's SCR shall thus be determined by the sum of the member's share of the syndicate SCR 'to ultimate'. Where a member participates on more than one syndicate, a credit for diversification is provided to reflect the spread of risk, but consistent with determining a SCR which reflects the capital requirement to cover a 1 in 200 year loss 'to ultimate' for that member.

The SCR represents the equivalent of minimum regulatory capital, as is required by the PRA and Lloyd's, and does not represent the amount of economic capital required to support and maintain Lloyd's financial strength, licence and ratings objectives. The SCR process produces a result that is then uplifted by Lloyd's (by 35% in 2020) of the member's SCR 'to ultimate'.

Each member may provide capital to meet its ECA either by assets held in trust by Lloyd's specifically for that member (Funds at Lloyd's), held within and managed within a syndicate (Funds in Syndicate) or as the member's share of the members' balances on each syndicate on which it participates.

Accordingly all of the assets less liabilities of the syndicate, as represented in the members' balances reported on the statement of financial position on page 17, are included in resources available to meet members' and Lloyd's capital requirements.

The Syndicate maintains models in accordance with this regime, and also operates an Own Risk & Solvency Assessment ("ORSA") process which it reports on at least annually.

6. Capital setting, capital management policies and objectives (continued)

Key elements of CMA's capital methodology include:

- risk identification;
- the articulation of risk bearing capacity and establishment of risk appetite;
- identification of capital requirement for all significant risks;
- sensitivity analysis and 'reasonableness checks';
- aggregation and correlation of risks;
- comparison with other benchmarks e.g. prior years' internal SCRs, standard formula SCR results, the PRA published calculations based on industry SCR submissions and market surveys/studies; and
- Board review and challenge.

To improve the risk management capability, and the assessment of capital requirements, CMA has developed a stochastic model to analyse the potential performance of its main underwriting operations. Stress and scenario analysis is also performed for those risks that cannot be easily modelled quantitatively and where more subjective judgement is required (for example, operational risk) as well as to challenge the output of the stochastic model.

Using its detailed measurement of risk exposures, the Syndicate allocates capital to support the business according to the risk appetite and expected returns. The Syndicate has complied with all capital requirements during the year.

CMA regularly reviews and enhances its risk management processes and their enabling governance structures to ensure that CMA can demonstrate continuous compliance with regulatory and Lloyd's requirements.

7. Segmental analysis

An analysis of the underwriting result before investment return is set out below:

2020	***Gross written premiums***	***Gross premiums earned***	***Gross claims incurred***	***Net operating expenses***	***[1]Re-insurance Balance***	***Total***
	£000	***£000***	***£000***	***£000***	***£000***	***£000***
Direct Insurance:						
Accident and health	47,284	48,024	(34,465)	(19,455)	548	(5,348)
Energy	13,185	15,818	(15,593)	(4,207)	2,356	(1,626)
Marine, Aviation & Transport	19,825	22,856	(22,101)	(6,061)	4,214	(1,092)
Fire & other damage to property	146,862	178,383	(128,683)	(72,524)	(23,593)	(46,417)
Third party liability	103,598	155,560	(121,883)	(46,671)	6,932	(6,062)
Pecuniary Loss	21,499	52,651	(93,387)	(16,677)	19,188	(38,225)
Others	20,027	9,796	(4,168)	(6,354)	(140)	(866)
Total Direct	372,280	483,088	(420,280)	(171,949)	9,505	(99,636)
Reinsurance inwards	154,147	175,575	(210,084)	(50,631)	6,028	(79,112)
Total	526,427	658,663	(630,364)	(222,580)	15,533	(178,748)

Current year underwriting results for those policies transferred to Lloyd's Brussels via Part VII transfer and subsequently reinsured back to the Syndicate have been reported in the same classes of business in which they were originally underwritten, as the effective date of the transfer was 30 December 2020, and in line with Society of Lloyd's guidance no movements were processed on these policies on 31 December 2020. In future years, results relating to these risks will be reported under the inwards Reinsurance class of business, reflecting the new contractual arrangement with Lloyd's Brussels

7. Segmental analysis (continued)

2019	*Gross written premiums*	*Gross premiums earned*	*Gross claims incurred*	*Net operating expenses*	*Re-insurance Balance*[1]	*Total*
	£000	*£000*	*£000*	*£000*	*£000*	*£000*
Direct Insurance:						
Accident and health	41,998	41,383	(28,195)	(16,733)	(1,969)	(5,514)
Energy	29,538	30,184	(19,890)	(8,747)	(6,653)	(5,106)
Marine, Aviation & Transport	25,283	35,262	(40,674)	(8,505)	5,900	(8,017)
Fire & other damage to property	174,924	175,224	(108,325)	(69,302)	(8,766)	(11,169)
Third party liability	213,232	199,295	(116,777)	(68,268)	(12,473)	1,777
Pecuniary Loss	49,581	44,905	(29,980)	(14,795)	2,614	2,744
Others	1,617	2,019	(1,193)	(992)	(11)	(177)
Total Direct	536,173	528,272	(345,034)	(187,342)	(21,358)	(25,462)
Reinsurance inwards	125,194	83,347	(47,739)	(31,901)	(11,580)	(7,873)
Total	661,367	611,619	(392,773)	(219,243)	(32,938)	(33,335)

[1]Reinsurance balance represents the (charge)/credit to the technical account from the aggregate of all items relating to reinsurance outwards. All premiums were concluded in the United Kingdom.

The geographical analysis of gross premiums written by destination is as follows:

	2020	*2019*
	£000	*£000*
US	219,686	269,154
UK	145,752	201,456
EU	19,442	49,028
Australia	18,547	33,687
Canada	14,604	31,550
Other	108,396	76,492
Total	526,427	661,367

In 2020 “other” represents the combined gross premium written in 158 territories not separately disclosed (2019:141 territories) none of which individually account for more than 2.5% of total premiums written.

8. Currency rates of exchange

	31 Dec 20	***Average for 2020***	*31 Dec 19*	*Average for 2019*
US $	1.37	1.28	1.32	1.28
Euro	1.12	1.13	1.18	1.14
Canadian $	1.74	1.72	1.72	1.69
Australian $	1.77	1.86	1.88	1.84

9. Net claims outstanding

The Syndicate has applied a similar approach at the current year end to that applied at the previous year end in establishing the technical provisions for claims outstanding reserves and reinsurers' share thereof. Included within net claims incurred of £473.6m (2019: £302.5m) is a deterioration of £7.9m (2019: deterioration of £8.4m) to claims reserves established at the prior year end principally due to unfavourable developments on Property, Third party liability and Accident and Health with partially offsetting favourable developments across the other classes.

10. Net operating expenses

	2020 £000	*2019 £000*
Commissions on direct business	114,170	161,589
Other acquisition costs	20,091	27,544
Change in deferred acquisition costs	52,309	(4,853)
Administrative expenses	27,083	26,674
Personal expenses (see note 11)	8,927	8,289
Total expenses – technical account	222,580	219,243
Loss / (profit) on exchange – non technical account	1,894	1,329
Total expenses	224,474	220,572

Administrative expenses include:

	2020 £000	*2019 £000*
Auditors' remuneration		
Audit of syndicate accounts	339	225
Other services pursuant to Regulations and Lloyd's Byelaws	183	179
Other non-audit services	80	72
Total audit and non-audit fees	602	476

11. Personal Expenses

	2020 £000	*2019 £000*
Members' standard personal expenses	4,508	4,267
Managing Agent's fee	4,419	4,022
Total	8,927	8,289

12. Staff numbers and costs

All staff are employed by a service company Canopius Services Limited ('CSL'). The following amounts were recharged to the Syndicate in respect of salary costs:

	2020	*2019*
	£000	*£000*
Wages and salaries	20,225	28,386
Social security costs	2,503	3,547
Pension contributions to money purchase schemes	1,277	1,178
Total	24,005	33,111

The average number of employees employed by CSL working on the Syndicate's affairs during the year was as follows:

	2020	*2019*
Underwriting	72	79
Insurance Services	45	22
Other	50	96
Total	167	197

13. Emoluments of the directors of the Managing Agents

The directors of CMA received the following aggregate remuneration charged to the Syndicate and included within net operating expenses:

	2020	*2019*
	£000	*£000*
Emoluments	1,643	690
Pension contributions to money purchase schemes	73	40
Total	1,716	730

Retirement benefits are accruing to 6 directors (2019: 9) under money purchase schemes.

The Active Underwriters received the following remuneration charged as a syndicate expense:

	2020	*2019*
	£000	*£000*
Emoluments	661	411
Total	661	411

Pension contributions amounting to £25k were charged to Syndicate 1861 on behalf of the active underwriters in 2020. (2019: £5k).

14. Net investment income recognised in profit or loss

	2020 **£000**	*2019* *£000*
Interest and similar income		
From financial instruments designated at fair value through profit or loss	5,302	3,048
Interest on cash at bank	-	-
Investment expenses	-	(355)
Total interest and similar income	5,302	2,693
Other income from investments designated at fair value through profit or loss		
Realised gains / (losses) on investments	667	6,072
Unrealised gains/ (losses) on investments	(1,101)	2,397
Total other gain / (loss)	(434)	8,469
Net investment return	4,868	11,162

	2020 **£000**	*2019* *£000*
Average amount of syndicate funds available for investment during the year	376,829	293,149
Gross aggregate investment return for the calendar year in Sterling	5,521	11,162
Gross calendar year investment yield	1.47%	3.81%

The Syndicate classifies its investments at fair value through profit and loss. Financial assets classified into this category form a portfolio of financial assets which may be sold to meet the cash flow requirements of the syndicate or as investment conditions change.

15. Other financial investments

	Fair value		**Cost**		**Listed**	
	2020 **£000**	*2019* **£000**	**2020** **£000**	*2019* **£000**	**2020** **£000**	*2019* **£000**
Shares and other variable yield securities and units in unit trusts	162,674	54,207	162,674	54,207	162,674	54,207
Debt and other fixed income securities	137,628	158,260	135,843	155,796	137,628	158,260
Derivative assets	1,419	-	1,419	-	1,419	-
Total	301,721	212,467	299,936	210,003	301,721	212,467

The Syndicate uses exchange traded derivatives and forward foreign exchange derivatives in order to hedge its exposure to interest rate and foreign currency risk.

The following derivative assets and liabilities were held at 31 December.

	Notional amount		**Fair value**	
	2020 **£000**	*2019* *£000*	**2020** **£000**	*2019* *£000*
Foreign exchange forward contracts asset	55,206	-	1,419	-
Foreign exchange forward contracts liabilities	52,268		(393)	
Total	107,474	-	1,026	-

Notes to the Financial Statements

16. Debtors arising out of direct insurance operations

	2020 £000	2019 £000
Due within one year		
Intermediaries[1]	179,712	314,672
	179,712	314,672
Due after more than one year and within five years		
Intermediaries	-	70
Total	-	314,742

17. Debtors arising out of reinsurance operations

	2020 £000	2019 £000
Due within one year		
Ceding insurers and intermediaries under reinsurance business[1]	81,280	962
Reinsurance recoverable on paid claims net of bad debt provision	26,327	24,986
	107,607	25,948
Due after more than one year and within five years		
Ceding insurers and intermediaries under reinsurance business	14	-
Total	107,621	25,948

[1] In 2019 £61.9m of accepted reinsurance pipeline debtors were included in debtors arising out of direct insurance operations which have been presented appropriately within debtors arising out of reinsurance operations in the current year. The comparatives have not been restated as we do not believe the reclassification would influence the economic decisions of users and is therefore not considered material.

18. Other debtors

	2020 £000	2019 £000
Due within one year		
Amounts due from group undertakings	4,983	712
Others	199	-
Total	5,182	712

19. Overseas deposits

Other assets include overseas deposits which are lodged as a condition of conducting underwriting business in certain countries.

For the 2019 calendar year, the movement in respect of overseas deposits within the Statement of Cash Flows was presented within cashflows in respect of investing activities. Within the 2020 calendar year, the equivalent movement is presented within cashflows in respect of operating activities.

20. Creditors arising out of direct insurance operations

	2020 £000	2019 £000
Due within one year		
Intermediaries	34,888	43,362
Total	34,888	43,362

21. Creditors arising out of reinsurance operations

	2020 **£000**	*2019* *£000*
Due within one year		
Reinsurance ceded	82,848	75,394
Total	82,848	75,394

22. Other creditors

	2020 **£000**	*2019* *£000*
Due within one year		
Amounts due to group undertakings	14,918	15,854
Derivative liabilities	393	-
Other	930	-
Total	16,241	15,854

23. Deferred acquisition costs

The reconciliation of opening and closing deferred acquisition costs is as follows:

	2020 **£000**	*2019* *£000*
At 1 January	126,688	128,669
RITC adjustment[1, 2]	29,459	(4,350)
Adjusted 1 January 2019	156,147	124,319
Change in deferred acquisition costs	(52,309)	4,853
Foreign exchange	(217)	(2,484)
At 31 December	103,621	126,688

24. Reconciliation of insurance balances

The reconciliation of opening and closing unearned premium provision is as follows:

	Gross		***Reinsurers' share***	
	2020 **£000**	*2019* *£000*	**2020** **£000**	*2019* *£000*
At 1 January	387,735	362,603	63,204	57,618
RITC adjustment[1,2]	61,527	(14,442)	314	(4,719)
Adjusted 1 January	449,262	348,161	63,518	52,899
Change in provision	(132,236)	49,748	(22,083)	12,703
Foreign exchange	(2,650)	(10,174)	(1,198)	(2,398)
At 31 December	314,376	387,735	40,237	63,204

[1] 2020 RITC adjustment: At 31 December 2019 the 2018 YOA of the Syndicate accepted the RITC of the 2017 years of account of Syndicates 5820 and 1206, two other Syndicates managed by Canopius Managing Agents Limited and with the same 100% capital provider. This was recorded as a balance sheet transaction in line with standard practice for a Lloyd's syndicate. An adjusted opening position has been presented to include the technical provisions in relation to Syndicate 5820 and 1206.

[2] 2019 RITC adjustment: At 31 December 2018 the 2016 & Prior years of account closed by way of an external reinsurance to close agreement. This was recorded as a balance sheet transaction in line with standard practice for a Lloyd's syndicate. An adjusted opening position has been presented to remove the brought forward technical provisions in relation to the 2016 & Prior years of account.

The reconciliation of opening and closing provision for claims is as follows:

	Gross		Reinsurers' share	
	2020 £000	2019 £000	**2020 £000**	2019 £000
At 1 January	456,646	510,238	98,844	160,776
RITC adjustment[1,2]	63,393	(241,918)	14,625	(94,288)
Adjusted 1 January	520,039	268,320	113,469	66,488
Change in provision	279,444	202,344	101,263	36,774
Foreign exchange	(28,512)	(14,018)	(8,995)	(4,418)
At 31 December	770,971	456,646	205,737	98,844

[1] 2020 RITC adjustment: At 31 December 2019 the 2018 YOA of the Syndicate accepted the RITC of the 2017 years of account of Syndicates 5820 and 1206, two other Syndicates managed by Canopius Managing Agents Limited and with the same 100% capital provider. This was recorded as a balance sheet transaction in line with standard practice for a Lloyd's syndicate. An adjusted opening position has been presented to include the technical provisions in relation to Syndicate 5820 and 1206.

[2] 2019 RITC adjustment: At 31 December 2018 the 2016 & Prior years of account closed by way of an external reinsurance to close agreement. This was recorded as a balance sheet transaction in line with standard practice for a Lloyd's syndicate. An adjusted opening position has been presented to remove the brought forward technical provisions in relation to the 2016 & Prior years of account.

25. Post balance sheet events

On the 4th January 2021, the Syndicate advanced funds of £10.9m to Lloyd's Brussels under the reinsurance agreement into segregated Part VII settlement bank accounts. These accounts remain an asset of the Syndicate and will be reported in future periods as deposits with ceding undertakings. The accounts will be managed by CMA on behalf of Lloyd's Brussels to settle Part VII claims.

On 12th February 2021 the Board of the Managing Agent authorised the closure of the 2018 year of account of the Syndicate, by way of an external reinsurance to close agreement, into the 2021 year of account of Premia Managing Agency Limited's Syndicate 1884. The contract was agreed on 18th February 2021 with a net reinsurance to close premium payable by the Syndicate of £273.0m.

On the closure of the 2018 year of account an amount of £36.6m will be called from third party funds deposited with the member to the 2018 year of account representing the uncalled losses at 36 months.

26. Pensions

Canopius Services Limited, 'CSL', operates defined contribution pension schemes for the employees of CSL, including those working on the Syndicate's affairs during the year. The assets of the schemes are held separately from those of CSL in independently administered funds. The amounts recharged to the Syndicate from CSL in respect of pensions are disclosed in Note 12.

27. Related parties

Lloyd's market regulations require that a managing agent be responsible for engaging underwriting staff and managing the affairs of each syndicate at Lloyd's on behalf of the syndicate members. The managing agent of the Syndicate is Canopius Managing Agents Limited ('CMA') following novation from AmTrust Syndicates Limited ('ASL') on 1 October 2019.

Throughout 2020 the expenses incurred in operating the Syndicate were incurred by the Canopius group service company and recharged under an intragroup service agreement with CMA on a basis that reflected the Syndicate's usage of resources. In 2019 expenses were incurred and recharged by AmTrust group service companies until 1 October 2019 and by a Canopius group service company thereafter.

27. Related parties (continued)

Group recharges are charged on a cost basis and predominantly represent recharges of staff costs for employees working on syndicate business as well as associated other administrative expenses including accommodation, professional fees and information technology. These recharges, included within amounts disclosed as net operating expenses, acquisition costs and claims incurred were as follows:

	2020 £000	2019 £000
AmTrust Central Bureau of Services Limited	-	253
AmTrust Management Services Limited ('AMSL')	-	40,214
Canopius Services Limited ('CSL')	54,377	15,662
Total expenses recharged	**54,377**	**56,129**

The following amounts were outstanding at 31 December 2020 and 31 December 2019:

	2020 £000	2019 £000
CSL	(12,257)	(15,662)
Total amount outstanding in relation to group recharges	**(12,257)**	**(15,662)**

Included within the recharges are amounts relating to the remuneration of directors of CMA and ASL. The following directors of CMA during the period were also directors of CSL during the period: M C Watson, N S Meyer (resigned from CSL board 1 November 2020) and L Davison.

CMA and CSL are both 100% subsidiaries of Canopius Holdings UK Limited ('CHUKL'). The following directors of CMA during the period were also directors of CHUKL during the period: M C Watson, N S Meyer and M P Duffy.

Members' expenses, being agent's fees and profit commission payable to the Managing Agent, and subscriptions and central fund contributions payable to Lloyd's, are charged on an underwriting year of account, rather than on a calendar year basis. For the 2020 underwriting year of account, CMA charged an agent's fee of 0.8% of stamp capacity. Within the financial statements, fees of £4.4m have been charged. At 31 December 2020 there are no unpaid fees.

Canopius Underwriting Bermuda Limited ("CUBL")

Canopius Underwriting Bermuda Limited ("CUBL") is an insurance service company that underwrites property reinsurance business on behalf of the Syndicate. Premiums written during 2020 totalled £5.0m (2019: £nil). At 31 December 2020, an amount of £0.3m was due from the Syndicate to CUBL (2019: £nil).

Canopius Asia Pte. Ltd ("CAPL")

Canopius Asia Pte. Ltd ("CAPL") trades as part of the Lloyd's Asia platform. CAPL underwrites Insurance and reinsurance lines, including and most notably, property, marine, energy and engineering, accident & health and treaty reinsurance business, on behalf of the Syndicate. Premiums written during 2020 totalled £31.3m (2019: £nil). At 31 December 2020, an amount of £2.0m was due from the syndicate to CAPL (2019: £nil).

Canopius Underwriting Agency Inc. ("CUAI")

Canopius Underwriting Agency Inc. ("CUAI") is a New York based coverholder that underwrites direct and facultative property, marine, financial and professional insurance. It also underwrites property treaty reinsurance business on behalf of the Syndicate. Premiums written during 2020 totalled £29.3m (2019: £nil). At 31 December 2020, an amount of £0.4m was due from syndicate to CUAI (2019: £nil).

CMA, CUBL, CAPL and CUAI are all indirect 100% subsidiaries of the same ultimate parent undertaking – refer to note 28.

2020 Year of Account "split stamp"
The 2020 year of account of the Syndicate was written on a split stamp basis with Syndicate 4444, another syndicate managed by CMA. Under this arrangement Syndicate 1861 underwrote 35% of each risk and Syndicate 4444 65%. The Syndicates similarly share the reinsurance programme protecting the 2020 year of account. No commissions or fees are payable between the syndicates under this arrangement.

Capital
Capital to underwrite the 2018 and 2019 years of account of the Syndicate is provided by Flectat 2 Limited (F2L) and capital to underwrite the 2020 year of account is provided by Flectat Limited (FL). The following directors of CMA during the period were also directors of F2L and FL during the period: M C Watson, M P Duffy and N S Meyer. F2L and FL are indirect 100% subsidiaries of the same ultimate parent undertaking – refer to note 28

Reinsurance to Close
On 13th February 2020 the Board of the Managing Agent authorised the closure of the 2017 years of account of Syndicates 5820 and 1206, both Syndicates with the same 100% capital provider F2L and managed by CMA, by way of reinsurance to close arrangements into Syndicate 1861's 2018 year of account effective 1 January 2020. The net reinsurance to close premium payable to the Syndicate from 5820 and 1206 was £80.5m. An amount of £3.4m was called from F2L representing the retained loss at closure of Syndicates 1206 and 5820.

Directors' interests
None of the directors nor the active underwriter participate on the Syndicate.

28. Immediate and ultimate parent undertaking and controlling party

As at 31 December 2020, Syndicate 1861 was managed by CMA. CMA's immediate UK parent is CHUKL, which is registered in England and Wales. CHUKL is part of CGL which is registered in Jersey. CMA's registered office is Gallery 9, One Lime Street, London EC3M 7HA.

The ultimate controlling parties of CGL are CCP GP Investors Holdings (Cayman) LP, CCP III Cayman GP Limited and CCP III SBS Cayman GP Limited.

29. Funds at Lloyd's

Every member is required to hold capital at Lloyd's which is held in trust and known as FAL. These funds are intended primarily to cover circumstances where syndicate assets prove insufficient to meet participating members' underwriting liabilities.

The level of FAL that a member is required to maintain is determined by CMA and Lloyd's based on compliance with PRA requirements. The determination of the FAL requirement has regard to a number of factors including the nature and amount of insurance contracts to be underwritten by the member and the assessment of the reserving risk in respect of business that has been underwritten. Since the assets in FAL are not owned by the syndicate, no amount has been shown in these financial statements by way of such capital resources. However, the managing agent is able to make a call on the members' FAL to meet liquidity requirements or to settle losses.